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A Survey Of The Legal Aspects Of Cooperative Apartment Ownership

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COMMENTS

A SURVEY OF THE LEGAL ASPECTS OF COOPERATIVE APARTMENT OWNERSHIP

INTRODUCTION

As more and more cooperative apartments appear throughout Florida, questions arise concerning what the "purchaser" of an apartment receives for the purchase price. What are his legal rights, his obligations and liabilities?

The objectives sought in "buying" an apartment in a cooperative organization assumedly are threefold: (1) to allow the purchaser to acquire the indicia of ownership of the apartment and a proportionate share of the public space, such as building and grounds; (2) to take advantage of the economic principle of cooperation, so that the cost of the property may be ratably shared and so that each owner will share in its management; and (3) to minimize the risk of personal liability to the members.[1]

The purpose of this comment is to present to the reader a description of the various available legal structures of the cooperative apartment, with a view toward selecting the type which more closely meets the objectives of a purchaser, and to determine the legal rights which the participants enjoy.[2]

JOINT TENANCY, TENANCY IN COMMON AND CONVEYANCE OF TITLE IN FEE

If the chief or sole purpose of the buyer is to own his apartment, three methods of organization are available. The first, apparently untried and

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1. Castle, *Legal Phases of Co-operative Buildings*, 2 So. CAL. L. REV. 1 (1928); McCullough, *Cooperative Apartments in Illinois*, 26 CHI.-KENT L. REV. 303 (1948).

2. For articles concerning the financing of cooperative apartments, see Anderson, *Cooperative Apartments in Florida: A Legal Analysis*, 12 U. MIAMI L. REV. 13 (1957); Bernstein, *Practical Problems in the Organization, Acquisition, Financing and Operation of Real Estate Cooperatives*, N.Y.U. 18TH INST. ON FED. TAX. 89 (1960); Note, *Co-operative Apartment Housing*, 61 HARV. L. REV. 1407 (1948); Note, *Federal Assistance in Financing Middle-Income Cooperative Apartments*, 68 YALE L. J. 542 (1959).

For articles concerning the tax aspects of cooperative housing, see Anderson, *supra*; Bachner, *Tax Problems of the Co-operative Apartment*, 5 PRAC. LAW. 77 (Nov. 1959); Bernstein, *supra*.

For an article concerning cooperative apartments and the "Blue Sky Laws" in Florida, see Anderson, *supra*.

highly impractical, is the joint tenancy.[3] Under this plan, the four unities of time, title, interest and possession are needed.[4] A joint tenant's interest does not descend to his heirs, cannot be devised, and is not subject to his wife's dower interest.[5] Finally, any joint tenant can, during his lifetime, convey his undivided interest to another and convert the estate into a tenancy in common.[6] The difficulties of this form are obvious and need not be discussed further.

The second method of organization which endows the purchaser with legal ownership of his apartment is the tenancy in common. In *Woods v. Krizan*,[7] the Court of Appeals for the Eighth Circuit upheld this form as a legal structure of a cooperative apartment. The court held that the acquisition and operation of an apartment building of twenty-one dwelling units by a group of twenty-one individuals for their occupancy under a tenancy in common, involved "inherent cooperative undertaking and organization"[8] within the provisions of the Housing and Rent Act.[9] Unlike the joint tenancy, unity of possesion is the only requisite.[10] Each tenant in common, although he owns only an undivided interest and has no exclusive right to possession, has a separate estate which he may alienate freely. Further, this estate is descendible to his heirs or devisable by his will.[11] The disadvantages of the tenancy in common outweigh the advantage of legal ownership of an apartment and its concurring benefits. First, there would be no way to enforce each owner's payment of his share of the financial obligations.[12] An apartment owned under a tenancy in common would render the apartment economically unmarketable. Perhaps the greatest single disadvantage of the tenancy in common, as well as the other

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3. 4 POWELL, THE LAW OF REAL PROPERTY ¶ 632, at 710 (1954).

4. Castle, note 1 *supra*. This means that all joint tenants must take at the same time, from the same instrument, the same proportionate share, and hold collectively the same undivided possession. BOYER, FLORIDA REAL ESTATE TRANSACTIONS § 20.01[1] (1961).

5. *Ibid.* It should be noted that the joint tenancy with right of survivorship is statutory in Florida and can be created only by express provision in the conveyance. FLA. STAT. § 689.15 (1961). Joint tenancies are no longer favored in the law. BOYER, *op. cit. supra* note 4.

6. *Ibid.*

7. 176 F.2d 667 (8th Cir. 1949).

8. *Id.* at 668.

9. Housing and Rent Act of 1948, ch 161, § 204(a), 62 Stat. 98. It does not appear significant that the owners who held undivided 1/21st interests in the property were considered cooperative owners only for the purpose of the cited statute since this form of cooperative ownership was suggested as a possible legal structure as early as 1928. Castle, note 1 *supra*. See note 17 *infra*.

10. BOYER, FLORIDA REAL ESTATE TRANSACTIONS § 20.01[1], at 435 (1961).

11. *Ibid.* The estate may, however, be partitioned, in which case the estate is terminated, each party owning thereafter his particular piece in severalty. BOYER, *op. cit. supra* note 10. If an estate in severalty is thereby created, the textual discussion regarding the conveyance of a title in fee would be applicable.

12. This disadvantage might be circumvented by the use of a declaration as found in Woods v. Petchell, 175 F.2d 202 (8th Cir. 1949).

forms in which title is in the apartment owner, is the unlimited liability of the owners.[13]

The third method of organization which participants in a cooperative apartment may adopt in order to acquire legal ownership, requires the conveyance of the apartment, in fee, to each tenant.[13a] The tenant acquires the legal ownership of the cubic footage constituting his apartment, and a tenancy in common is established as to the areas used in common.[14] Each individual would have easements of support for his own apartment and, for protection in the event of partition, easements of right-of-way on the common portions.[15] An example of a participant holding title to his individual apartment is found in *Woods v. Petchell.*[16] The owner of a building sold the six apartments within, deeding to each person a private apartment and an undivided one-sixth interest in the common property. Accompanying each contract of sale was a "standard plural residence declaration" (hereinafter referred to as the declaration). It was provided in the declaration that there would be a managing trustee who would have complete charge of the property, including the power to estimate annually all expenses and to charge each apartment owner one-sixth of the total, payable in twelve monthly installments. It was further provided that any owner could be evicted upon failure to pay his pro rata share of the expenses. There was nothing which called for officers to be elected (other than the managing trustee) or for stock to be issued. There was no provision in the declaration concerning the leasing or renting of the units to the purchasers. Title to each apartment passed by deed, will or descent and not by assignment of a lease or stock certificate. The issue to be resolved by the court was whether the plan was a "cooperative association" within the purview of the Housing and Rent Act. If so, the act would not allow the apartment owners to evict the tenants of the former owner of the building.[17] The

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13. Yourman, *Some Legal Aspects of Co-operative Housing,* 12 LAW & CONTEMP. PROB. 126 (1947); Note, *Co-operative Apartment Housing,* 61 HARV. L. REV. 1407 (1948).

13a. For an excellent article on a new "twist" in cooperative apartments, see Ramsey, *Condominium: New Look to an Old Concept,* 28 LEGAL BULL. 33 (1962).

14. 4 POWELL, *op. cit. supra* note 3; 1 AMERICAN LAW OF PROPERTY § 3.10, at 199 (Casner ed. 1952).

15. *Ibid;* Note, *Co-operative Apartment Housing,* 61 HARV. L. REV. 1407 (1948). The latter author also suggests a plan whereby each individual owns an area between established horizontal and vertical planes which includes the common facilities as well as his own apartment. All the owners are given cross-easements of support and right-of-way upon the areas owned by the others. He points out that in both cases each owner is under a contractual liability to share the expense of maintaining the common facilities.

16. 175 F.2d 202 (8th Cir. 1949).

17. Housing and Rent Act of 1948, ch. 161, § 204(a), 62 Stat. 98. This section provided that cooperative owners could not evict tenants of the former building owner unless 65% of the cooperative owners were already in possession. The legislative history of this section reveals an attempt to curb the so-called "cooperative racket" which had grown up in an attempt to circumvent the rent law. See Marks & Marks, *Coercive Aspects of Housing Cooperatives,* 42 ILL. L. REV. 728 (1948); see also Annot., 10 A.L.R.2d 249, 324-27 (1950).

defendant owners argued that this was not a cooperative, since no provision was made for an organization of the purchasers, by-laws, stock, or a proprietary lease.[18] The court held this was a cooperative association, explaining that the plan in question provided an equivalent substitute for every feature claimed to be absent.[19]

While offering a more feasible method of organization than the first two systems, inherent difficulties are present in the conveyance of the title in fee. One writer suggests that the use of cross-easements is cumbersome and sacrifices unified control of the building.[20] The caveat has been put forth that there is a risk with this form of organization because the owners are unprotected against tenants who are unable to bear their share of the expenses[21] or that financial responsibility could be attained, if at all, only through a complicated series of agreements, uncertain in operation and lacking in "teeth."[22] Although the use of a declaration in connection with the deed and contract of sale, seen in *Woods v. Petchell*,[23] would appear to combat this latter aspect, the problems do not end there. The sale of an apartment would leave the remaining owners unprotected against the purchase by an undesirable,[24] and subleasing would be difficult to control. The individual owners would have the impractical, if not the insoluble, problem of having their apartments insured separately and assessed separately for purposes of taxation.[25]

THE TRUST[26] AND CORPORATE FORMS

There are two forms of organization which more closely conform to the alleged objectives of the cooperative apartment buyer. Of the two, the

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18. Defendants were contending, in effect, that this was not a cooperative since not in the corporate form. See textual discussion *infra*.

19. The court reasoned that the declaration served the purpose of by-laws and created an organization of the purchasers of interests in each structure with power to elect a managing trustee. The deeds given the purchasers subject to the restrictions in the declaration served as stock certificates. It further pointed out that it was not necessary that a purchaser of stock or other evidence of interest in a cooperative be entitled to a proprietary lease before the statute would be applicable; it was sufficient if each owner was entitled by virtue of his ownership to possession of a particular unit. Woods v. Petchell, 175 F.2d 202, 207-08 (8th Cir. 1949).

20. Note, *Co-operative Apartment Housing*, 61 HARV. L. REV. 1407 (1948); see 1 AMERICAN LAW OF PROPERTY § 3.10, at 199 (Casner ed. 1952).

21. *Ibid. But see*, Note, *Federal Assistance in Financing Middle-Income Cooperative Apartments*, 68 YALE L.J. 542, 600 (1959), in which this form of organization is suggested as a possible answer to the alleged problem of financial interdependence prevalent when the title to property is vested in one entity.

22. Castle, *Legal Phases of Co-operative Buildings*, 2 So. CAL. L. REV. 1 (1928).

23. 175 F.2d 202 (8th Cir. 1949); see text accompanying note 16 *supra*.

24. This refers to one who might disturb an otherwise harmonious relationship as well as one undesirable because of race, religion, etc. Since Shelley v. Kraemer, 334 U.S. 1 (1948) would preclude the latter restrictions in a declaration due to their unenforceability, the *Woods v. Petchell* form of organization would be ineffectual in combatting this problem.

25. See Castle, *Legal Phases of Co-operative Buildings*, 2 So. CAL. L. REV. 1 (1928); Note, *Co-operative Apartment Housing*, 61 HARV. L. REV. 1407 (1948).

26. The business trust is legitimate in Florida under FLA. STAT. ch. 609 (1961).

corporate form has been overwhelmingly the more popular.[27] No attempt will be made to set forth in detail the procedures involved in the formation of the two types of cooperatives.[28] The writer will describe only those techniques which distinguish these forms, since the principles of operation of both are the same.[29]

Under the trust form, an express trust is established, and the title to the property is conveyed to the trustee.[30] The trustee, in turn, may either issue certificates of beneficial interest to the individual apartment owners,[31] or he may issue the whole beneficial interest to the organizer of the project, who assigns to the purchasers their respective shares.[32] The rights of the beneficiary are governed by the declaration of trust,[33] which also prescribes the obligations assumed by the apartment owners.[34] The declaration may provide that any beneficial interest may be pledged or mortgaged by a written instrument. It may further provide that in the event any beneficiary defaults in his payments, the trustee may sell that beneficiary's interest and apply the proceeds to the obligation, distributing the balance to the person so entitled.[35]

For a discussion of business trusts generally, see 16 FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS §§ 8227-74 (repl. 1942).

27. McCullough, *Co-operative Apartments in Illinois*, 26 CHI.-KENT L. REV. 303 (1948).

28. For articles concerning the formation of cooperative apartments, see Anderson, *Cooperative Apartments in Florida: A Legal Analysis*, 12 U. MIAMI L. REV. 13 (1957); Bernstein, *Practical Problems in the Organization, Acquisition, Financing and Operation of Real Estate Cooperatives*, N.Y.U. 18TH INST. ON FED. TAX. 89 (1960); Bernstein, *Formation of a Co-operative Apartment Venture*, 5 PRAC. LAW. 69 (Nov. 1959).

29. 4 POWELL, THE LAW OF REAL PROPERTY ¶ 632, at 710 (1954).

30. McCullough, *Co-operative Apartments in Illinois*, 26 CHI.-KENT L. REV. 303 (1948).

31. These certificates convey a specified fractional interest in the trust together with the right of permanent occupancy to a named apartment in accordance with the trust terms. The obligations of the beneficiary under the trust, as set forth in the declaration of trust, will be reiterated in the certificates. Yourman, *Some Legal Aspects of Cooperative Housing*, 12 LAW & CONTEM. PROB. 126 (1947).

32. Castle, *Legal Phases of Co-operative Buildings*, 2 So. CAL. L. REV. 1 (1928). The trust entity also makes leases with the tenant certificate holders substantially in the same form as proprietary leases. Hennessey, *Co-operative Apartments and Town Houses*, 1956 U. ILL. L.F. 22.

33. For sample forms, see Castle *supra* note 32, at 10 n.20; Hennessey, *supra* note 32, at 43.

34. The declaration states the purpose of the trust and sets forth in great detail the provisions thereof. The primary purpose, as actually stated, is the allotment to the beneficiaries of the exclusive rights of occupancy of their individual apartments, together with the use of the common space and facilities, for the life and subject to the provisions of the trust. The provisions include: (1) the obligations of the beneficiary to pay his pro rata share of the expenses of operation; (2) the requirement that the beneficial owners observe the rules imposed by the trust concerning the use of the apartments and common facilities; (3) an agreement not to use the apartment or permit it to be used for any purpose prohibited by the declaration of trust or by-law; (4) the obligation of the beneficiary to surrender possession upon termination of his rights under the declaration; and (5) a provision that an attempt to transfer any portion of the beneficiary's interest except in accordance with the terms of the trust and with the consent of the trustee will be ineffective. McCullough, *Co-operative Apartments in Illinois*, 26 CHI.-KENT L. REV. 303, 307 (1948).

35. Castle, note 32 *supra*.

The trust declaration may provide for a "Board of Governors" elected from, and by, the apartment owners. This board acts in an advisory capacity to the trustee in the supervision of the operation of the building and the estimation of the annual budget. However, the ultimate control and management *must* remain with the trustee.[36]

A majority of the holders of beneficial interests may empower the trustee to encumber the trust property or to sell unnecessary portions of it for the benefit of the trust. The power to terminate the trust also lies with the majority and, if terminated, the property is sold and the proceeds are paid proportionately to the beneficiaries.[37]

While the trust form of organization has considerable flexibility,[38] its greatest single disadvantage lies in the fact that its use either results in the relinquishment of control by the members or, if the control is exercised, there is a risk of personal liability. This choice results from the fact that even in those states which recognize business trusts, the right of the members to manage their own affairs exposes them to personal liability as partners, in relation to the obligations of the trust.[39] Florida seems to be no exception.[40]

The last form of organization to be considered is the corporation. The promoter of the venture organizes the corporation,[41] which acquires the building and land, usually subject to a mortgage, to be used for the cooperative. The prospective apartment owner buys a block of shares corre-

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36. That is, for purposes of maintaining limited liability this requisite would be necessary. See textual discussion *infra*. McCullough, *Co-operative Apartments in Illinois*, 26 CHI.-KENT L. REV. 303 (1948).

37. *Ibid.*

38. Jones, *Business Trusts in Florida — Liability of Shareholders*, 14 U. FLA. L. REV. 1 (1961).

"[T]he use of such trusts may eliminate certain formal requirements of corporate existence and operation as well as permit some freedom of action not ordinarily available to corporations. For example, no capital stock tax returns, annual reports, or franchise taxes would be necessary, and limitations of purely formal character in taking, evidencing, and reporting corporate action, would be simplified." Hennessey, *Co-operative Apartments and Town Houses*, 1956 U. ILL. L.F. 22, 30. However, trusts are ordinarily treated in the same manner as corporations for income tax and for most security regulation purposes. *Ibid.* See also Anderson, *Cooperative Apartments in Florida: A Legal Analysis*, 12 U. MIAMI L. REV. 13 (1957).

39. Yourman, *Some Legal Aspects of Cooperative Housing*, 12 LAW & CONTEMP. PROB. 126 (1947). "While the risk of personal liability is undesirable, the alternative to it under the trust form, the relinquishment of democratic control, is equally unsatisfactory. It would remove mutuality of responsibility in the management of the project and would almost certainly invite an apathy which would be destructive of community spirit and morale." *Id.* at 128.

40. For an article considering the problem of shareholder liability under the business trust in Florida, see Jones, *Business Trusts in Florida — Liability of Shareholders*, 14 U. FLA. L. REV. 1 (1961).

41. The corporate cooperative apartment is organized in Florida under the provisions of FLA. STAT. ch. 608 (1961). There appears to be no reason why it could not also be organized under the corporation not for profit statute, FLA. STAT. ch. 617 (1961). The advantage of the latter statute would be important only if federal assistance were contemplated for purposes of insuring the mortgage. See Note, *Federal Assistance in Financing Middle-Income Co-operative Apartments*, 68 YALE L.J. 542 (1959).

sponding to the value of the apartment he will occupy. Ownership of the shares, in turn, entitles him to a proprietary lease.[42]

Three instruments are needed to effectuate the corporate cooperative, and the three, read together, comprise the contract between the corporation and the individual owners.[43] As is the case in any business corporation, this form of organization requires a charter[44] and a set of by-laws. These instruments contain, for all practical purposes, the same provisions found in the usual trust declaration. The directors elected by the shareholders have the same rule-making and assessment powers[45] as the trustee under the business trust, including the power to sell the stock in the event the stockholder defaults in his assessed payments. This is made possible by a provision in the by-laws[46] which gives the corporation a prior lien upon the shares registered in the name of a stockholder for debts due the corporation.[47]

The by-laws may provide that there shall be no transfer of shares by the individual owners without the consent of the directors or a specified

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In some states, cooperatives are governed by cooperative corporation statutes. See Abbot v. Bralove, 81 F. Supp. 532 (D.D.C. 1948), *aff'd*, 176 F.2d 64 (D.C. Cir. 1949), which contains a discussion of a non-stock corporate form. The only advantage of this form is that membership in a non-stock corporation may be considered not a security under the Securities and Exchange Act, and registration may be avoided. Bernstein, *Practical Problems in the Organization, Acquisition, Financing and Operation of Real Estate Cooperatives*, N.Y.U. 18TH INST. ON FED. TAX. 89 (1960).

42. Castle, *Legal Phases of Co-operative Buildings*, 2 So. CAL. L. REV. 1, 4-9 (1928). See 1 AMERICAN LAW OF PROPERTY § 3.10 (Casner ed. 1952); Bernstein, *Practical Problems in the Organization, Acquisition, Financing and Operation of Real Estate Cooperatives*, N.Y.U. 18TH INST. ON FED. TAX. 89 (1960); McLaughlin, *The Co-operative Apartment Corporation*, 5 PRAC. LAW. 74 (Nov. 1959).

43. In Tompkins v. Hale, 172 Misc. 1071, 15 N.Y.S.2d 854 (Sup. Ct. 1939) an attempt was made by the corporation to modify the proprietary lease by a two-thirds vote of the shareholders. The court held that the original contract of the tenants who owned shares in the corporation, which fixed the rights and obligations of the parties, could not be modified without the unanimous consent of all the parties.

44. The charter should state that the corporation is providing homes for the stockholders who are entitled to a proprietary lease because of their holdings. It should include the power to hold, sell, lease or mortgage real estate with reference to the specific building to be sold as a cooperative. There should be a waiver of pre-emptive rights so that if additional stock is issued, the corporation controls it. The charter sets the number of directors, usually three to fifteen depending on the number of apartments. McLaughlin, *The Co-operative Apartment Corporation*, 5 PRAC. LAW. 74 (Nov. 1959). The charter should provide that no stockholder shall be entitled to receive any distribution not out of earnings and profits. See INT. REV. CODE OF 1954, § 216(b)(1)(C).

45. Under the corporate form, each member is assessed proportionately to the number of shares held.

46. This provision may be backed up by a special shareholder's agreement accompanied by a provision in the minutes and the proprietary lease referring to this agreement. The agreement may be required as a condition to the issuance of the proprietary lease, and it will provide for the stockholder to make a collateral pledge of his shares of stock, appropriately endorsed and deposited with the corporation or in escrow to secure the payment of his obligations and his performance of the conditions provided for in the by-laws and proprietary lease. If such an agreement is used, there should be a notation of its existence on the stock certificates, and formal corporate approval of the agreement should be endorsed on the certificates themselves. Hennessey, *Co-operative Apartments and Town Houses*, 1956 U. ILL. L.F. 22, 29.

47. See sources cited in note 42 *supra*. *In re* Pitts' Estate, 218 Cal. 184, 22 P.2d 694 (1933) held that a corporation which maintained an apartment house in which the

proportion of the stockholders,[48] and that there shall be no alienation of shares except as an entirety.[49] The by-laws may place a further restriction on subletting and assigning without proper authorization and may provide that authorization will be granted only if the assignee has assumed the obligations of his assignor in writing.[50]

The third instrument within the corporation framework is the proprietary lease. This is the most important instrument to the purchaser, for, without it, he has no right of occupancy of his apartment. Stock ownership alone will not suffice.[51]

The proprietary lease, usually a long term instrument,[52] is subject to defeasance for failure to pay the assessed share of the costs, or for breaking the house rules or breach of the covenants contained within the lease[53] or by-laws.[54] The main difference between this lease and an ordinary long-

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members of the corporation held apartments retained a lien on the property "leased" (the apartments) for that part of his proportionate share of the purchase price of the building which remained unpaid by the "lessee."

48. In the alternative, an option may be given to the corporation to purchase the stock at the same terms at which it is offered any other purchaser. Castle, *Legal Phases of Co-operative Buildings*, 2 So. CAL. L. REV. 1 (1928). See *In re* Pitts' Estate, note 47 *supra*. Repurchase of the stock by the corporation is governed in Florida by FLA. STAT. § 608.13(9)(b) (1961). For articles regarding the power of the corporation to repurchase its own stock see Blackstock, *A Corporation's Power to Purchase Its Own Stock and Some Related Problems*, 13 TEXAS L. REV. 442 (1935); Dodd, *Purchase and Redemption by a Corporation of Its Own Shares: The Substantive Law*, 89 U. PA. L. REV. 697 (1941).

Under the trust form, the repurchase of the certificates of a deceased tenant may be possible without encountering the numerous statutory requirements which complicate repurchase of corporate stock by corporations. Note, *Co-operative Apartment Housing*, 61 HARV. L. REV. 1407 (1948).

For a discussion of the validity of a regulation interfering with the free transferability of stock, see Note, *Cooperative Apartments—a Legal Hybrid*, 13 U. FLA. L. REV. 123 (1960). For cases validating the restraint on free transferability of shares in a cooperative apartment corporation, see 68 Beacon St., Inc. v. Sohier, 289 Mass. 354, 194 N.E. 303 (1935). In Penthouse Properties, Inc. v. 1158 Fifth Ave., Inc., 256 App. Div. 685, 11 N.Y.S.2d 417 (1939) it was stated that these provisions are neither invalid nor unenforceable as in restraint of alienation, when it appears that the restrictions imposed were legal, reasonable and appropriate to the lawful purpose to be attained. See also FLA. STAT. § 608.13(12) (1961).

49. This is done in the effort to tie the stock and lease together and to keep the ownership of the apartments in the hands of their occupants. Castle, note 48 *supra*.

50. See 68 Beacon St., Inc. v. Sohier, 289 Mass. 354, 194 N.E. 303 (1935); 1165 Fifth Ave. Corp. v. Alger, 288 N.Y. 67, 41 N.E.2d 461 (1942).

51. McCullough, *Co-operative Apartments in Illinois*, 26 CHI.-KENT L. REV. 303 (1948).

52. C. G. J. Corp. v. Hurwitz, 123 So.2d 44 (Fla. App. 1960) (ninety-nine years); *In re* Miller's Estate, 205 Misc. 770, 130 N.Y.S.2d 295 (Surr. Ct. 1954) (twenty-one years). It may be for a term of perpetual duration. Wardman Constr. Co. v. Flynn, 54 F.2d 831 (D.C. Cir. 1931); Hennessey, *Co-operative Apartments and Town Houses*, 1956 U. ILL. L.F. 22. However, proprietary leases have been drawn to run from year to year. The advantage of this form is that an undesirable tenant may be removed in a shorter time. But the security of the long-term lease has made it the preferred form. McCullough, *Co-operative Apartments in Illinois*, 26 CHI.-KENT L. REV. 303, 316-17 (1948). Most modern proprietary leases run from 20 to 50 years, some of them with renewal privileges. McLaughlin, *The Co-operative Apartment Corporation*, 5 PRAC. LAW. 74 (Nov. 1959).

53. The provisions contained in the by-laws will normally be incorporated in the proprietary lease so as to become terms of the lease to which the lessees subscribe.

54. Hennessy, *Co-operative Apartments and Town Houses*, 1956 U. ILL. L.F. 22.

term lease is the provision for "rent."[55] Although the form may vary somewhat,[56] "rent" under the proprietary lease will often have three components: (1) a nominal annual rent;[57] (2) a "further rent," fixed annually by the board of directors and based on the maintenance and operation costs of the building, mortgage payments and tax assessments;[58] and (3) an "additional rent" which may be levied against the individual tenant, if that tenant fails to maintain properly the interior of his apartment, necessitating the corporation to perform the work.[59]

It is of the utmost importance that all the provisions outlining the rights and obligations of the shareholder under the proprietary lease, whether used with the corporate or trust form, be particularized completely. Since the contract, consisting of all the instruments, will be construed strictly by the courts, the subjective intent of the parties when entering their agreement becomes relatively unimportant.[60] For instance, upon the death of the tenant, his shares of stock[61] pass as personalty to his personal representative.[62] Provision must be made in the proprietary lease to bind the

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55. *Ibid.*

56. See, *e.g.*, Paul Laurence Dunbar Apartments, Inc. v. Nelson, 136 Misc. 561, 241 N.Y. Supp. 354 (N.Y.C. Munic. Ct. 1930), wherein rent consisted of the tenant's proportionate share of the actual maintenance charges, as called for in the lease, and larger monthly installments on the purchase price, as called for in a "subscription agreement."

57. 1165 Fifth Ave. Corp. v. Alger, 288 N.Y. 67, 41 N.E.2d 461 (1942) ($1.00 annual rent).

58. See Smith v. Feigin, 273 App. Div. 277, 77 N.Y.S.2d 229, *aff'd*, 298 N.Y. 534, 80 N.E.2d 668 (1948). This rental might also be used for maintaining a reserve fund. Teitelbaum, *Representing the Purchaser of a Cooperative Apartment*, 45 ILL. B.J. 420 (1957). One obvious purpose for this fund would be the repurchase of stock. See note 47 *supra*. Another purpose of the reserve fund would be to carry the burden of a financially distressed shareholder during a period of depression in order to save the remaining, and financially responsible, members from loss of their interests due to foreclosure of the mortgage. However, if funds are retained to be applied to expenses of a subsequent period, rather than returned to the stockholders, the excess over the amount qualifying as capital contributions plus an amount equal to the operating expenses will be subject to tax. Taylor, *Tax Aspects of Real Estate Cooperatives*, N.Y.U. 18TH INST. ON FED. TAX. 97 (1960).

It should be noted that each portion of the rent which is attributable to the mortgage interest and to the real estate taxes is deductible for income tax purposes by the tenant-owner if the building falls within the purview of INT. REV. CODE OF 1954, § 216(b)(1)(D).

59. Teitelbaum, *supra* note 57, at 421-22.

For a case involving the liability of the tenant-owner to the landlord for these "rents," see Paul Laurence Dunbar Apartments, Inc. v. Nelson, 136 Misc. 561, 241 N.Y. Supp. 354 (N.Y.C. Munic. Ct. 1930). For cases involving the liability of the tenant-owner to a receiver appointed in foreclosure of the mortgage for these "rents," see Greenebaum Sons Bank & Trust Co. v. Kingsbury, 248 Ill. App. 321 (1928); Prudence Co. v. 160 West Seventy-Third St. Corp., 260 N.Y. 205, 183 N.E. 365 (1932); Greenberg v. Colonial Studios, 279 App. Div. 555, 107 N.Y.S.2d 87, *reversing mem.* 105 N.Y.S.2d 494 (Sup. Ct. 1951). See also New York Life Ins. Co. v. 1325 Astor St. Bldg. Corp., 325 Ill. App. 536, 60 N.E.2d 257 (1945).

60. McCullough, *Co-operative Apartments in Illinois*, 26 CHI.-KENT L. REV. 303 (1948).

61. This is also applicable to a certificate of beneficial interest under the trust form.

62. *In re* Miller's Estate, 205 Misc. 770, 130 N.Y.S.2d 295 (Surr. Ct. 1954) held that a testamentary devise of "all the real estate owned by me" did not include, in the

administrator to the covenants of the lease and by-laws, restricting his use and limiting his power of sale in the same manner as the decedent was bound. Likewise, similar limitations must be placed upon his widow in those states in which she has a statutory dower right in her husband's personal property. This is the case in Florida.[63] In *1165 Fifth Avenue Corp. v. Alger*[64] the corporation sought to hold the defendant liable for his share of the expenses. A provision in the proprietary lease restricted the assignment of stock without the consent of the board of directors of the corporation, unless assigned to the wife, widow, child or grandchild of the lessee, or to a trustee for the benefit of any such person. The defendant transferred his stock and ninety-nine year lease, without the plaintiff's consent, to a trustee for his grandson for life or until the grandson should reach the age of twenty-five, at which time the corpus was to be distributed to him. The lower court ruled for the plaintiff, holding the trust invalid, since the only assets of the trust estate were the stock and the lease. The trustee did not assume any personal obligations under the lease, and the trust might end before the lease expired. In reversing the judgment, the court of appeals stated that the lease allowed the assignment, and placed no restriction upon the financial responsibility of the assignee. The defendant was released from liability and the assignee substituted in spite of the other reasons set out by the lower court.

Although less flexible than the business trust, and encumbered with certain formal requirements absent from the trust form,[65] the corporation gives to its members the limited liability sought, without sacrificing their voice in the management. But is the ownership which the cooperative apartment purchaser seeks present in the corporate form?[66]

It has been stated that it is the shares in the corporation that are sold, and despite a vernacular usage to the contrary, the apartment is not sold, but is leased under the so-called proprietary lease.[67] The situation unequivocally created by this instrument is that the association owns the property, and the stockholders are lessees with no more legal[68] or equitable title than stockholders in any other corporation.[69] The lease creates a relationship

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absence of proof to the contrary, a disposition of stock in an incorporated cooperative apartment and of a proprietary lease.

63. FLA. STAT. § 731.34 (1961).

64. 288 N.Y. 67, 41 N.E.2d 461 (1942).

65. Hennessey, note 38 *supra*.

66. Although the cases to be discussed concern cooperatives organized under the corporate form, it seems likely that the conclusions to be drawn would be equally applicable to the trust form, since the principle of both forms is the same. See POWELL, *op. cit. supra* note 29.

67. People *ex rel.* McGoldrick v. Sterling, 283 App. Div. 88, 126 N.Y.S.2d 803 (1953). See Abel v. Paterno, 245 App. Div. 285, 281 N.Y. Supp. 58 (1935).

68. *But see*, Moses v. Boss, 72 F.2d 1005 (D.C. Cir. 1934).

69. Schaffer v. Eighty-One Hundred Jefferson Ave. E. Corp., 267 Mich. 437, 255 N.W. 324 (1934).

of landlord and tenant in no way different from that created by any standard lease for a residential apartment.[70]

This restatement is somewhat harsh, however, and courts have tempered this lack of absolute ownership with some indicia of that coveted legal right. In three New York cases[71] determining the legal status of cooperative apartment owners, the issue was raised as to whether these owners were landlords within the meaning of applicable statutes which allowed a landlord to dispossess a tenant. Those statutes required the landlord to have title to the area in question in order to bring "dispossess proceedings." Those courts declared that the stockholders are, *in effect*, regarded as the owners of the rooms to be occupied by them.[72] When the stockholder's premises is rented to another the former stands in the position of a landlord-lessor.[73] The object in the cooperative plan is, so far as possible, to constitute the persons to whom space in the building has been assigned as owners of this space. *Where the circumstances are such as to warrant it*, the courts will pierce the corporate veil, looking behind the corporate fiction.[74]

The emphasized words, then, become the key to the solution of the ownership question. If it is the desire of the court to base its determination upon "substantial justice, rather than on legal principle,"[75] there are circumstances when a court is warranted in holding that the stockholder is an owner. Practically speaking, the true status of the cooperative buyer seems best summarized by Judge Cayton in *Hicks v. Bigelow*:[76]

> Such purchaser is more than a mere tenant or lessee. She has certain proprietary rights which a mere tenant does not have. She has most of the *attributes* of an owner. She has a voice in the management and operation of a building. She has a voice in the selection or approval of other tenant-owners. She has a voice, too, in the important matter of any proposed sale or mortgage of the

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70. Marks & Marks, *Coercive Aspects of Housing Cooperatives*, 42 ILL. L. REV. 728, 736-37 (1948).

71. Smith v. Feigin, 273 App. Div. 277, 77 N.Y.S.2d 229, *aff'd*, 298 N.Y. 534, 80 N.E.2d 668 (1948); 542 Morris Park Ave. Corp. v. Wilkins, 120 Misc. 48, 197 N.Y. Supp. 625 (Sup. Ct. 1922); Curtis v. Le May, 186 Misc. 853, 60 N.Y.S.2d 768 (N.Y.C. Munic. Ct. 1945).

72. *Ibid.*

73. Curtis v. Le May, 186 Misc. 853, 60 N.Y.S.2d 768 (N.Y.C. Munic. Ct. 1945). *Contra*, Braislin, Porter & Baldwin, Inc. v. Sawdon, 68 N.Y.S.2d 774 (Eastchester J. Ct. 1946). Criticizing the *Curtis* case, the court said that if the law was to recognize distinctions between proprietary lessees and other lessees, it was for the legislature or the court of last resort.

See Martin v. Rutland Court Owners, Inc. 171 F.2d 798 (D.C. Cir. 1948), in which the corporation was held *not* to be the landlord of an apartment owner's sublessee and therefore not under a duty to repair.

74. Smith v. Feigin, 273 App. Div. 277, 77 N.Y.S.2d 229, *aff'd*, 298 N.Y. 534, 80 N.E.2d 668 (1948).

75. Braislin, Porter & Baldwin, Inc. v. Sawdon, 68 N.Y.S.2d 774, 776 (Eastchester J. Ct. 1946).

76. 55 A.2d 924 (D.C. Munic. Ct. App. 1947).

> property. More important, she has the exclusive, personal right to occupy her particular apartment.[77]

"But in legal theory," concluded Professor Lesar, "the corporation is distinct from its shareholders, no one of whom has a right to receive legal title to any specific property of the corporation under the better-drawn plans, and it is necessary that this distinction be observed in order to carry out the purposes of the cooperative."[78] In essence, the cooperative purchaser has no absolute ownership, but merely the attributes or indicia of ownership.

HOMESTEAD TAX EXEMPTION

The remaining legal right to be considered is the right of the owner-tenant to the homestead tax exemption available under the Florida Constitution.[79] The law in Florida appears settled that the exemption allowed to "any one dwelling house" will be construed strictly. Thus, in *Overstreet v. Tubin*[80] the court determined that the two owners of separate apartments in a duplex were entitled to but one five thousand dollar exemption between them. Similarly, the district court of appeal, in *Gautier v. State*,[81] rejected the claims of the owners of four apartments in a four-unit building, allowing each but a proportionate part of the tax exemption.[82] Therefore, if otherwise entitled, the apartment dwellers will divide the exemption proportionately among the number of apartments within the "one dwelling house."

In a recent opinion by the Florida Attorney General,[83] the homestead exemption of owners of cooperative apartments was considered and clarified. His views are hereinafter set forth.

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77. *Id.* at 926. (Emphasis added.) See *In re* Pitts' Estate, 218 Cal. 184, 22 P.2d 694 (1933).

78. 1 AMERICAN LAW OF PROPERTY § 3.10, at 200 (Casner ed. 1952). The purpose of the organization is to approach individual ownership as nearly as possible in a situation where the only practical solution is common operation and management, and the number of the occupants' shares are determined by the value of the apartments they occupy. *Ibid.* The reason for this distinction is to retain for the corporation the remedies that are available to the ordinary landlord in the event the lessee defaults in his obligations. People *ex rel.* McGoldrick v. Sterling, 283 App. Div. 88, 126 N.Y.S.2d 803 (1953).

79. FLA. CONST. art. X, § 7: "Every person who has the legal title or beneficial title in equity to real property in this State and who resides thereon and in good faith makes the same his or her permanent home, . . . shall be entitled to an exemption from all taxation . . . up to the assessed valuation of Five Thousand Dollars on the said home and contiguous real property . . . . [N]o such exemption of more than Five Thousand Dollars shall be allowed to any one person or on any one dwelling house, nor shall the amount of the exemption allowed any person exceed the proportionate assessed valuation based on the interest owned by such person. The Legislature may prescribe appropriate and reasonable laws regulating the manner of establishing the right to said exemption."

80. 53 So.2d 913 (Fla. 1951).

81. 127 So.2d 683 (Fla. App. 1961).

82. Judge Pearson, dissenting, stated: "Where real property is described as a portion of a lot and block so that it may be separately assessed and levied upon, the incident that the building thereon has a party wall in common with a building on another portion of the lot and block does not, in ordinary language, deprive the first building of its character as a dwelling house. I would affirm in order to afford the Supreme Court an opportunity to re-examine the precedent." *Id.* at 685.

83. Fla. Att'y Gen. Op. 061-143 (Sept. 12, 1961).

Under the tenancy in common and trust forms of ownership, there is sufficient title in the owners (legal in the former, equitable in the latter) to bring them within the title interest limitation. However, in the corporate form the legal and equitable title is vested in the corporation, and the interest of the apartment owner is that of a stockholder. Under the applicable Florida statute,[84] this interest is personalty, and the owner's claim for an exemption would fail.[85]

The attorney general went on to state that the conveyance of title to an apartment was sufficient to support an application for homestead tax exemption, but his opinion was based on the fact that the conveyance was a legal title in the nature of a perpetual lease or easement rather than the conveyance of real property to the extent of a deed of conveyance of the building. Therefore, as long as the conveyance is not for a term of years, in which case personal property is involved, the individual owners may receive their homestead exemption proportionately with the others.

CONCLUSION

If one had his choice when "buying" a cooperative apartment as to which type he would take, there seems to be little doubt that he would quickly narrow his choice to either the corporate or trust form. Of these, the more discriminating buyer would select the corporate form, since he and his fellow tenants would not have to decide between the distasteful alternatives of unlimited liability or limited control. The lack of homestead tax exemption would receive little consideration at least in a many-unit dwelling where, once divided among the numerous apartments, the exemption would be negligible. The limitations on ownership should be of no great influence in deciding between the available forms, since, if it is a true cooperative apartment which is desired, there must be limitations placed upon the owners no matter which form is employed. These limitations on ownership are not undesirable. It is, however, important that the prospective purchaser knows of the limitations and is not misled by glamorous offers to own an apartment.

The current court interpretations of the constitutional provision allowing a homestead tax exemption appear unrealistic and dated. The constitution allows the exemption to "every person who has the legal title or beneficial title in equity to real property . . . *and who resides thereon and*

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84. FLA. STAT. § 608.42 (1961).

85. The 1961 Florida Legislature passed an act amending FLA. STAT. § 100.241(1) (1959) which provides that tenant-stockholders of cooperative apartment corporations should be deemed freeholders for voting purposes. Fla. Laws 1961, ch. 61-332. Since the Legislature is able to make a law such as this, there would seem to be no reason why they could not also enact a law to the effect that the interest of a tenant-stockholder in a cooperative apartment corporation is realty for purposes of homestead tax exemption.

in good faith makes the same his . . . permanent home . . . ."[86] If a person puts forth a sum of money equivalent to that put forth by a home buyer, and he has the intent to reside in his apartment permanently, there is no logical reason why he should not be treated on the same footing as the home buyer. The rationale of the *Overstreet* case[87] is to the effect that if the individual owners of a duplex were each granted homestead exemptions, then it might be carried further to include more than two units, "together occupying less than the one-half acre contemplated under our Constitution as being the extent of only one homestead in cities . . . , and which would result in serious revenue losses to the local taxing authorities."[88] The loss of revenue argument does not necessarily follow, however, for the homestead exemption to cooperative owners would act as an incentive to prospective purchasers and to builders, and a flourishing, rather than a diminishing, economy could be foreseen.

The success of cooperative apartments in Florida, coupled with the permanency of the owners in their occupancy, lead this writer to the conclusion that cooperatives are not, in all probability, just a fad. Therefore, if the Florida Constitution will not permit the full homestead tax exemption because of the acreage requirements contemplated as a homestead in 1885,[89] there should be no hesitation in righting this lack of foresight by amendment. But if, as Judge Pearson's dissent in the *Gautier* case[90] would seem to indicate, the solution lies in a re-examination by the supreme court of the precedent set in *Overstreet v. Tubin*,[91] it can only be hoped that on its next opportunity to consider this question, the court will be influenced by the apparent nature of cooperative apartments as permanent homes for the owners and will give the "one dwelling" provision a more realistic interpretation.

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86. FLA. CONST. art. X, § 7. (Emphasis added.) See note 79 *supra*.
87. Overstreet v. Tubin, 53 So.2d 913 (Fla. 1951).
88. *Id.* at 915.
89. FLA. CONST. art. X, § 1.
90. Gautier v. State, 127 So.2d 683 (Fla App. 1961).
91. 53 So.2d 913 (Fla. 1951).